

# STATE OF CALIFORNIA

Report to the California State Legislature

## PROPERTY TAX APPORTIONMENTS

*Calendar Year 2003*



STEVE WESTLY  
California State Controller

June 2004



**STEVE WESTLY**  
**California State Controller**

June 25, 2004

**To the Members of the State Legislature  
and the Citizens of California:**

I am pleased to present the Property Tax Apportionments report for calendar year 2003. This report, prepared pursuant to *Government Code* Section 12468, is intended to help mitigate problems associated with the counties' apportionment and allocation of property tax revenues.

The audits completed by the State Controller's Office in 2003 found the audited counties to be generally in compliance with the legal requirements for allocating property tax revenues. However, this report notes specific problem areas relative to individual counties.

I hope you find the report informative and useful for future policy decisions.

Sincerely,

*Original signed by*

**STEVE WESTLY**  
California State Controller

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# Overview

## Introduction

This report presents the results of 16 audits of county property tax apportionments and allocations completed by the State Controller's Office (SCO) in calendar year 2003. The following counties were audited: Alameda, El Dorado, Glenn, Imperial, Kern, Kings, Los Angeles, Mendocino, Mono, Nevada, San Francisco, Santa Barbara, Sierra, Siskiyou, Sonoma, and Sutter. *Government Code* Section 12468 requires that such audits be conducted periodically for each county according to a prescribed schedule based on county population. The purpose of the audits is to help mitigate problems associated with property tax apportionment and allocation.

Except for the findings and recommendations noted in this report, all audited counties complied with the requirements for the apportionment and allocation of property tax revenues.

## Background

After the passage of Proposition 13 in 1978, the California State Legislature enacted new methods for allocating and apportioning property tax revenues to local government agencies and public schools. The main objective was to provide local agencies with a property tax base that would grow as assessed property values increase. These methods have been further refined in subsequent laws passed by the Legislature.

One key law was Assembly Bill 8, which established the method of allocating property taxes for fiscal year 1979-80 (base year) and subsequent fiscal years. The methodology is commonly referred to as the AB 8 process or the AB 8 system.

Property tax revenues that local governments receive each fiscal year are based on the amount received the prior year plus a share of the property tax growth within their boundaries. Property tax revenues are then apportioned and allocated to local agencies and schools using prescribed formulas and methods defined in the *Revenue and Taxation Code*.

The AB 8 process involved several steps, including the transfer of revenues from schools to local agencies and the development of the tax rate area annual tax increment growth factors (ATI factors), which determine the amount of property tax revenues allocated to each entity (local agency and school). The total amount allocated to each entity is then divided by the total amount to be allocated to all entities to determine the AB 8 factor (percentage share) for each entity for the year. The AB 8 factors are computed each year for all entities using the revenue amounts established in the prior year. These amounts are adjusted for growth annually using ATI factors.

Subsequent legislation has removed revenues generated by unitary and operating nonunitary property from the AB 8 system. This revenue is now allocated and apportioned under a separate system.

Other legislation established an Educational Revenue Augmentation Fund (ERAF) in each county. Most local government agencies are required to transfer a portion of their property tax revenues to the ERAF. The fund is subsequently allocated and apportioned by the county auditor according to instructions received from the local superintendent of schools or chancellor of community colleges.

Taxable property includes land, improvements, and other properties that are accounted for on the property tax rolls, which are primarily maintained by the county assessor. Tax rolls contain an entry for each parcel of land, including parcel number, owner's name, and value. The types of property tax rolls are:

- *Secured Roll*—Property that, in the opinion of the assessor, has sufficient value to guarantee payment of the tax levies and that, if unpaid, can be satisfied by the sale of the property by the tax collector.
- *Unsecured Roll*—Property that, in the opinion of the assessor, does not constitute sufficient “permanence” or have other intrinsic qualities to guarantee payment of taxes levied against it.
- *State-Assessed Roll*—Utility properties, composed of unitary and nonunitary value, assessed by the State Board of Equalization.
- *Supplemental Roll*—Property that has been reassessed due to a change in ownership or the completion of new construction, where the resulting change in assessed value is not reflected in other tax rolls.

## Audit Program

The property tax audit program began on July 1, 1986, under *Revenue and Taxation Code* Section 95.6 (now *Government Code* Section 12468). The statute mandates that the State Controller periodically perform audits of the allocation and apportionment of property tax revenues by counties and make specific recommendations to counties concerning their property tax administration. However, the State Controller's authority to compel resolution of its audit findings is limited to those findings involving an overpayment of state funds.

Overpayment of state general fund money is recoverable by the State under several provisions of law (e.g., *Education Code* Section 42237.7 et seq., and *Government Code* Section 12420 et seq.). In addition, the State Controller has broad authority to recover overpayments made from the State Treasury. If an audit finds overpayment of state funds, and the state agency that made or authorized the payment does not seek repayment, the SCO is authorized to pursue recovery through a variety of means (e.g., *Government Code* Sections 12418 and 12419.5). The specific remedy employed by the SCO depends on the facts and circumstances of each situation.

To carry out the mandated duties of the State Controller, the SCO developed and implemented a comprehensive audit program that includes, but is not limited to, a detailed analysis of past and current requirements of property tax laws and an examination of property tax records, processes, and systems at the county level.

These property tax apportionment audits have identified and aided in the correction of property tax underpayments to public schools. The underallocation of property taxes by individual counties to their public schools results in a corresponding overpayment of state funds to those schools by the same amount. This, in turn, causes public schools in other counties to receive less state funding because the total funds available are limited. Subsequent legislation forgave some counties for underpayments to schools without requiring repayment or assessment of penalties. However, the legislation required that the cause of the underallocations, as identified by the audits, be corrected.

## Audit Scope

Each audit encompasses an evaluation of a county's property tax apportionment methodology, allocation procedures, and compliance with applicable laws and regulations. The auditors used procedures considered necessary to provide a basis for reporting on the areas examined. In conducting the audits, the auditors focused on the following areas to determine if:

- The apportionment and allocation of annual tax increment (ATI) was in accordance with *Revenue and Taxation Code* Sections 96-96.5;
- The methodology for redevelopment agencies' base-year calculations and apportionment and allocation of ATI was in accordance with *Revenue and Taxation Code* Sections 96.4 and 96.6 and *Health and Safety Code* Sections 33670 through 33679;
- The effect of jurisdictional changes on base-year tax revenues and ATI was in accordance with *Revenue and Taxation Code* Section 99;
- The apportionment and allocation of property tax revenues from supplemental assessments was in accordance with *Revenue and Taxation Code* Sections 75.60 through 75.71;
- The apportionment and allocation of state-assessed unitary and operating nonunitary property taxes was in accordance with *Revenue and Taxation Code* Section 100;
- The computation and apportionment of property tax revenues to low- and no-tax cities was in accordance with *Revenue and Taxation Code* Section 98;
- The computation and collection of local jurisdictions' property tax administrative costs was in accordance with *Revenue and Taxation Code* Sections 95.2 and 95.3;

- The computation and apportionment of property tax revenues to the ERAF was in accordance with *Revenue and Taxation Code* Sections 97 through 97.3; and
- For eligible counties, the computation of the county credit against the county's ERAF shift was in accordance with *Revenue and Taxation Code* Sections 97.3(a)(5) and 97.36.

## Conclusion

The property tax allocation and apportionment system is generally operating as intended. In the interest of efficiency and cost control for both the counties and the State, the Summary of Findings and Recommendations in this report is submitted to assist in initiating changes that will help improve the system.

# Summary of Findings and Recommendations

## Introduction

Except for the findings and recommendations cited in this report, the audit reports issued in 2003 indicated that the counties complied with the legal requirements for the apportionment and allocation of property tax revenues. However, problem areas were identified and are described below. Recommendations to resolve the problems are included with the individual county findings.

## Unresolved Prior Audit Findings

As part of the audit process, auditors review the prior audit report to determine issues that may require follow-up action. Procedures are undertaken to determine whether previously noted findings have been resolved. Unresolved prior audit findings are restated in the current audit.

The SCO restated findings for five counties with unresolved prior audit findings.

## Computation of Annual Tax Increment Factors

The *Revenue and Taxation Code* requires that each jurisdiction in a tax rate area (TRA) be allocated property tax revenues in an amount equal to the property tax revenues it was allocated in the prior fiscal year. The difference between this amount and the total amount of property tax assessed in the current year is known as the annual tax increment. The computation of the annual tax increment results in a percentage that is used to allocate growth in assessed valuation to local government jurisdictions and schools in a county from the base-year forward. *Revenue and Taxation Code* Sections 96 through 96.5 prescribe this methodology. (Some exceptions to this allocation are contained in the *Revenue and Taxation Code* for specified TRAs.)

The SCO noted findings for five counties in this area.

- Three counties had factor computation errors, noted in prior audits, that had not been fully corrected.
- Two counties had increment computation errors due to incorrect prior year revenue amounts being used.

## Jurisdictional Changes

*Revenue and Taxation Code* Section 99 prescribes the procedures required to make adjustments for the apportionment and allocation of property taxes resulting from changes in jurisdictional controls or changes in responsibilities of local government agencies and schools. The statute requires specific documentation that takes into consideration services and responsibilities when changes occur.

The SCO noted findings for six counties in this area.

- Two counties improperly adjusted the TRA increment factors for jurisdictions not affected by the change.
- Two counties made errors in adjusting the assessed value of affected TRAs.



- One county did not properly follow exchange resolutions and made errors in adjusting the assessed value of affected TRAs.
- One county had a one-year delay in the implementation of changes.

## **Supplemental Property Tax Apportionments**

When a revaluation of property occurs during the fiscal year due to changes in ownership or completion of new construction, supplemental taxes are usually levied on the property. *Revenue and Taxation Code* Sections 75.70, 75.71, and 100.2 provide for the apportionment and allocation of these supplemental taxes.

The SCO noted findings for five counties in this area.

- Two counties did not apportion supplemental taxes in the timeframe prescribed.
- Two counties improperly included redevelopment agencies in the supplemental apportionment factor computations.
- One county used an incorrect supplemental apportionment factor file for the years' apportionments.

## **Supplemental Property Tax Administrative Fees**

Counties, upon the adoption of a method identifying the actual administrative costs associated with the supplemental roll, are allowed to charge an administrative fee for supplemental property tax collections. This fee is not to exceed 5% of the supplemental taxes collected.

The SCO noted findings for four counties in this area.

- Three counties did not properly document supplemental tax costs for reimbursement.
- One county carried forward costs that had already been reimbursed.

## **Redevelopment Agencies**

The legal requirements for the apportionment and allocation of property tax to redevelopment agencies are found in *Revenue and Taxation Code* Sections 96.4 and 96.6 and *Health and Safety Code* Sections 33670 through 33679. California community redevelopment law entitles a community redevelopment agency to all of the property tax revenue realized from growth in values since the redevelopment project's inception, with specified exceptions.

The SCO noted findings for seven counties in this area.

- Three counties had unresolved project base year revenue errors. Two of these were previously noted and continue to be a problem.
- Two counties included ERAF in redevelopment pass-through computations, and one of them did not properly distribute all annual tax increment to the proper agencies.
- One county did not properly compute annual tax increment using all assessed values.
- One county accepted incomplete statements of indebtedness.

## Unitary and Operating Nonunitary Property Taxes

The process for allocating and apportioning property taxes from certain railroad and utility companies functions through the unitary and operating nonunitary tax system employed by the State Board of Equalization. Unitary properties are those properties on which the State Board of Equalization “may apply the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee” (i.e., public utilities and railroads). The *Revenue and Taxation Code* further states, “Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee.” *Revenue and Taxation Code* Section 100 prescribes the procedures required to allocate unitary and operating nonunitary property taxes beginning in fiscal year (FY) 1988-89.

The SCO issued findings for seven counties in this area.

- Three counties did not compute excess revenue increases correctly. One of these counties also excluded the ERAF while one other continues to apportion unitary revenue to the special district augmentation fund.
- One county did not include redevelopment agencies in the unitary apportionment computations.
- One county excluded the ERAF and redevelopment from the apportionment computations and computed debt rates incorrectly.
- One county failed to carry forward the prior year revenue correctly.
- One county failed to correct errors previously noted in the base year computation.

## Property Tax Administrative Fees

Counties are allowed to collect from each appropriate jurisdiction that jurisdiction’s share of the cost of assessing, collecting, and apportioning property taxes. *Revenue and Taxation Code* Section 95.3 prescribes the requirements for computing and allocating property tax administrative fees. The assessor, tax collector, and auditor generally incur county property tax administrative costs. The county is generally allowed to be reimbursed for these costs.

The SCO noted findings for four counties in this area.

- Three counties failed to properly reduce costs to offset revenues received.
- One county used an incorrect cost/share ratio to collect costs from local agencies.

## Educational Revenue Augmentation Fund

The legal requirements for the local agency shift of property tax revenues to the ERAF are found in *Revenue and Taxation Code* Sections 97 through 97.3. Beginning in FY 1992-93, each local agency was required to shift an amount of property tax revenues to the ERAF using formulas prescribed by the *Revenue and Taxation Code*. The property tax revenues in the ERAF are subsequently allocated to schools and community colleges using factors supplied by the county superintendent of schools or chancellor of the California community colleges.

Since the passage of the ERAF shift requirements, numerous bills have been enacted that affect the shift requirements for various local government agencies. One bill of particular interest was AB 1589 (Chapter 290, Statutes of 1997). This bill primarily addressed three areas related to the ERAF shift: (1) ERAF shift requirements for certain county fire funds for FY 1992-93 (*Revenue and Taxation Code* Section 97.2(c)(4)(B)); (2) a special provision for counties of the second class when computing the ERAF shift amount for county fire funds in FY 1993-94 (*Revenue and Taxation Code* Section 97.3(c)(4)(A)(I)); and (3) ERAF shift requirements for county libraries for FY 1994-95 and subsequent years. After the passage of AB 1589, the State Controller requested advice from the California Attorney General regarding the application of Chapter 290. The Attorney General responded in May 1998.

The Attorney General advised that the amendment to *Revenue and Taxation Code* Section 97.2(c)(4)(B) significantly narrowed the scope of the exemption granted by the code section and was to be given retroactive application. The result is that many counties and special fire protection districts that were able to claim an exemption under the section as it formerly read lost the exemption retroactive to FY 1992-93. Consequently, those counties and special districts were required to shift additional funds to the county ERAF.

In response to the advice by the Attorney General, and noting the severe fiscal impact the loss of the exemption would have on local government agencies, the State Controller recommended that legislation be considered to restore the exemption previously granted to fire protection districts and county fire funds that was lost as a result of Chapter 290. Subsequently, the Legislature enacted AB 417 (Chapter 464, Statutes of 1999), restoring the exemption to fire districts that had been lost after the passage of Chapter 290, Statutes of 1997.

The SCO issued findings for nine counties in this area.

- Four counties had minor computation errors resulting in underpayment to the ERAF, and one of these is restated from a prior audit.
- Three counties had continuing uncorrected errors that had been previously reported.
- Two counties had overpayment computation errors that will require ERAF refunds to a few local agencies.

## **ERAF Shift Credit**

*Revenue and Taxation Code* Sections 97.3(a)(5) and 97.36 allow a credit against the county's required ERAF shift. Counties that first implement the alternative procedure for the distribution of property tax revenues authorized by Chapter 2 (commencing with Section 4701) of Part 8 during FY 1993-94, or a subsequent fiscal year, are allowed a credit against their required ERAF shift. The credit is limited to the amount of any increased revenues allocated to a "qualifying school entity" that would not have been allocated but for the implementation of the alternative procedure.

For purposes of determining the ERAF shift credit, the Legislature defined a qualifying school entity as a "school district, county office of education, or community college district that is not an excess tax school entity as defined in Section 95.1" (*Revenue and Taxation Code* Section 97.3[a][5]). Most counties, when computing the credit, instead used the definition of "school entity" contained in Section 95(f), which included the ERAF. The inclusion of the ERAF in the credit computation, in some instances, dramatically increased the credit. The State Controller's legal counsel opined that counties must use the definition of qualifying school entity when computing the credit. Noting the severe fiscal impact of this situation on many counties, the State Controller delayed proceeding on this matter until legislation could be introduced to revise the definition of qualifying school entity. The Legislature subsequently enacted AB 838 (Chapter 649, Statutes of 1999), which included the ERAF as a qualifying school entity.

Chapter 649 also contained a special provision for counties of the sixteenth class. This provision allowed counties of the sixteenth class to compute the amount of the shift credit based upon their historical method of allocating property taxes.

The SCO noted no findings in this area.

## **Tax Equity Allocation**

*Revenue and Taxation Code* Section 98 and the *Guidelines for County Property Tax Administration Charges and No/Low Property Tax Cities Adjustment*, provided by the County Accounting Standard and Procedures Committee, provide a formula to increase the amount of property tax received by a city that had either no or low property tax revenues.

The SCO noted no findings in this area.

# Findings of Individual County Audits

## Introduction

The findings and recommendations included below are presented as they were stated in the County Property Tax Apportionment and Allocation reports issued by the SCO in calendar year 2003. Unless otherwise indicated, the counties agreed with the findings and recommendations.

The findings and recommendations listed below are solely for the information and use of the California Legislature, the respective counties, the Department of Finance, and the SCO, and are not intended to be and should not be used by anyone other than those specified parties. This restriction is not intended to limit distribution of this report or the respective audit reports, which are a matter of public record.

## Alameda County (July 1, 1997, through June 30, 2002)

### Follow-up on Prior Audit Findings

Findings noted in the prior audit report, dated July 31, 1998, have been satisfactorily resolved by the county.

### FINDING 1— Jurisdictional changes

The county property tax system computes jurisdictional change TRA factors based on revised revenue. The factors should be computed using the agreed-upon exchange agreement.

The legal requirements for jurisdictional changes are found in *Revenue and Taxation Code* Section 99. A jurisdictional change involves a change in organization or boundaries of local government agencies and school districts. Normally, these are service area or responsibility changes between the local jurisdictions. As part of the jurisdictional change, the local government agencies are required to negotiate any exchange of base year property tax revenue and annual tax increment. After the jurisdictional change, the local agency whose responsibility increased receives additional annual tax increment, and the base property tax revenues are adjusted according to the negotiated agreements.

#### Recommendation

During the audit fieldwork, the county corrected the formula in the property tax system to comply with the jurisdictional change agreements. The SCO reviewed and accepted the documents.

#### County's Response

The County's calculations of TRA factors under jurisdictional change are governed by the terms of the tax exchange agreement. In comparing the method of the State vs. the County, the result yields insignificant variance. The differences in some cases can be one hundredth thousand of a cent or less. The County however agrees to modify the AB 8 system to comply with the State's recommended method and procedure.

**FINDING 2—  
Supplemental  
Property Tax  
Apportionment**

The supplemental revenue collection from July 2001 through November 2001 was apportioned using prior year AB 8 factors rather than the current factors.

The legal requirements for supplemental roll property tax apportionment and allocation are found in *Revenue and Taxation Code* Sections 75.60 through 75.71 and 100.2. When there is a change in assessed property value due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

Recommendation

During the audit fieldwork, the county corrected the revenue apportionment amount. The SCO reviewed and accepted the correction.

County's Response

The County has corrected the amounts of the supplemental revenue apportioned.

**FINDING 3—  
Unitary and operating  
nonunitary  
apportionment**

The county did not abolish the Special District Augmentation Fund (SDAF) in the unitary and operating nonunitary property tax apportionment system. In addition, when unitary and operating nonunitary property tax revenues grew by more than 2% over the preceding year, the excess revenues were apportioned using the administrative cost apportionment factors.

Requirements for the apportionment and allocation of property tax to RDAs are found in *Revenue and Taxation Code* Sections 96.4 and 96.5. California Community Redevelopment Law generally entitles a community redevelopment agency to all of the property tax revenues that are realized from growth in values since the redevelopment project's inception.

Recommendation

The SDAF is defunct by law and should be removed from the unitary and operating nonunitary property tax apportionment system. The factors for this fund should be returned to the contributing agencies. When the revenue of unitary and operating nonunitary property tax revenue exceeds 102% of the revenue available in the prior year, the excess should be distributed using the prior year AB 8 factors.

County's Response

The State Legislature enacted SB 1135 in July 1993, which repealed Section 98.6 through 98.68 of the Revenue and Taxation Code that established the Special District Augmentation Fund. This bill did not address how the SDAF contribution from the Unitary Tax Roll is to be distributed. The County's Board of Supervisors has the authority to determine how to treat SDAF.

For the 2003/04 Fiscal Year, our office will make recommendations that the Board of Supervisors remove SDAF from the unitary tax apportionment and return to each district a proportionate amount based on its contributed to SDAF.

The AB 8 system for Alameda County does not include RDA agencies. Because of this, we cannot use the prior AB 8 factors to allocate the excess of 102% unitary and operating non-unitary taxes. The excess unitary taxes are distributed by applying the tax administration cost apportionment factors. The tax administration factors consist of the AB 8 factors that have been modified to include the RDA agencies.

#### SCO's Comment

The use of tax administration factors for the apportionment of excess of 2% unitary taxes is acceptable if those factors do not include any other revenue amounts such as unitary and operating nonunitary tax revenue.

#### **FINDING 4— Property tax administrative costs**

The county supplemental administrative cost system carried forward prior unreimbursed costs to be reimbursed in subsequent fiscal years. These costs were also included in the regular property tax administrative cost reimbursement system calculation.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in *Revenue and Taxation Code* Section 100.

Unitary properties are those properties on which the Board of Equalization “may apply the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee” (i.e., public utilities and railroads). The *Revenue and Taxation Code* further states, “Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee.”

In FY 1988-89, the Legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The unitary and operating nonunitary base year was established and formulas were developed to compute the distribution factors for the fiscal years that followed.

#### Recommendation

The county agreed with the finding and has taken the necessary step to correct the administrative cost reimbursement system. The corrected system will be used in the current fiscal year.

#### County's Response

The County agrees to include the supplemental costs in the tax administrative cost reimbursement system only if the SA costs are greater than the SA revenue. If the SA revenue exceeds the SA costs, the negative Net SA costs will reduce the cumulative SA cost.

**FINDING 5—  
Redevelopment  
agencies**

When the total roll is negative for secured or unsecured value within the RDA, the negative amount is excluded from the calculation of the RDA increment.

Requirements for the reimbursement of county property tax administrative costs are found in *Revenue and Taxation Code* Section 95.3. County property tax administrative costs are incurred by the assessor, the tax collector, the assessment appeals board, and the auditor. The county is allowed, depending on the fiscal year and any corresponding exclusions, to be reimbursed by local agencies and public schools for these administrative costs.

**Recommendation**

The county should calculate RDA increment by including all roll values.

**County's Response**

As mentioned previously, our AB 8 system does not include RDA in the calculation of the 1% apportionment factors. The redevelopment assessed value increments are calculated outside of the AB 8 system. Our calculation of the RDA increment is in accordance to generally accepted guidelines of the State of California Accounting Standards and Procedures for Counties.

If the overall valuation for the current year is less than the base year values, no increment is due and it is excluded from the calculation. The Accounting Standards and Procedures Manual Section 18.07 states that this comparison is to be done separately for the current secured and unsecured rolls.

In surveying other County's methods for calculating RDA increment, we discovered that a majority of them include all roll values.

Therefore, in compliance with the State's recommendation, our office will hereby include all roll values when calculating RDA increments.

**El Dorado County (July 1, 1996, through June 30, 2002)****Follow-up on Prior  
Audit Findings**

Findings noted in the prior audit, dated March 31, 1998, have been satisfactorily resolved by the county, with the exception of an ERAF issue that is restated in this audit.

**FINDING—  
Educational Revenue  
Augmentation Fund  
(ERAF)**

It was noted in the prior audit, and restated here, that the City of Placerville transferred all of its property tax base revenue to the El Dorado County Fire District in FY 1993-94 to cover the city's fire suppression needs. As part of the agreement, the 1992-93 ERAF shift of 9% plus future growth for the city was assumed by the fire district; however, the city's per capita shift and the additional FY 1993-94 shift were not passed on to the district or retained by the city. As a result, the ERAF is underallocated by \$1,002,690 plus growth (Schedule 1).



Requirements for the local agency shift of property tax revenues to the ERAF are generally found in *Revenue and Taxation Code* Sections 97.1 through 97.3. Beginning in FY 1992-93, each local agency was generally required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF are subsequently allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was generally determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was generally determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts was generally determined by shifting the lesser of 10% of that district's total annual revenues as shown in the FY 1989-90 edition of the State Controller's *Report on Financial Transactions Concerning Special Districts* or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties was generally determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, was generally determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting this amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting this amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding this amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift was generally determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net

current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;

- Adjusting this amount for growth; and
- Adding this amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years subsequent to FY 1993-94, the amounts determined are adjusted for growth, annually to determine the ERAF shift amounts for that year.

### Recommendation

The ERAF shift amounts assessed to the City of Placerville must be fully paid with growth, and future ERAF contributions shall be paid as specified in the statute.

### County's Response

Absent an agreement between the City of Placerville and the State Controller's Office, the El Dorado County Auditor-Controller is prepared to execute the following. Effective FY2003/04, the Auditor-Controller will adjust the AB-8 factors for the annual amount shown on the draft audit (adjusted for prior years' growth) for the purpose of shifting property tax revenues from the City of Placerville to the ERAF fund. Effective FY2003/04, the FY2002/03 AB-8 factors will be adjusted to reflect the annual ERAF shift (with growth). These factors will be used for any "prior year" property tax revenues during FY2003/04. Effective FY2003/04, the FY2003/04 AB-8 factor will be adjusted to reflect the annual ERAF shift. These factors will be used for any "current year" property tax revenues during FY2003/04. The process will then be repeated for future years.

The draft audit report has calculated ERAF shift amounts (\$111,410 per year without prior years' growth) exceeding the City of Placerville's annual current year property tax allocations (approximately \$72,000 for FY2001/02). This leaves an "unfunded" annual amount of approximately \$39,000 (without prior years' growth) using FY2001/02 as an example. I am unable to determine a lawful method for the El Dorado County Auditor-Controller to collect any future years' unfunded annual ERAF shift amounts from the City of Placerville's non-property tax revenues. Therefore, the County of El Dorado would be placed in significant legal peril if this office were to pursue collection of future years' unfunded annual ERAF shift amounts. El Dorado County concludes that the ERAF statutes do not authorize the Auditor-Controller to use non-property tax revenue to repay the State for prior year ERAF shift payments as a matter of law. El Dorado County recommends that the State and the City of Placerville meet to work out a repayment agreement, which the Auditor-Controller will thereafter implement with the concurrence of both parties.

Absent an agreement between the City of Placerville and the State Controller's Office, the El Dorado County Auditor-Controller is prepared to execute the following. Effective FY2003/04, the Auditor-Controller will calculate and apply the ERAF shift growth for the City of Placerville as per the attached schedule. This schedule will be used for the base ERAF shift for FY2003/04 AB-8 factor

calculations. This same schedule will also be used for the base ERAF shift to make adjustments to the FY2002/03 AB-8 factors to be used effective FY2003/04.

In regards to the draft audit report's amount of \$111,410 for the FY1993/94, the El Dorado County Auditor-Controller believes that the amount was transferred to the ERAF fund based on the AB-8 factors that were calculated in September 1993 and used throughout FY1993/94. This office will need to review apportionment records from FY1993/94 and all general ledger entries of the City of Placerville to confirm this situation. This office will advise the State Controller's Office and the City of Placerville with the results as soon as the review is completed.

For the amounts on the draft audit report's schedule for the annual ERAF shift amounts (with growth) for FY1994/95 through FY2002/03, the County of El Dorado recommends that the State and the City of Placerville reach an agreement regarding repayment of the ERAF funds owed to the State. Any agreement between the two parties that requires implementation by the Auditor-Controller's staff will be implemented the concurrence of both parties.

#### SCO's Comment

As was stated in the previous audit, it is the auditor's understanding that the City of Placerville agreed to transfer its share of property tax revenue to the El Dorado County Fire District and retain only a small factor for growth (ATI). The district agreed to assume the city's required ERAF shift amount related to percentage of property taxes received. There was apparently no agreement on the city's required population shift amount to the ERAF. The net result of the agreement is that the city agreed to transfer property tax revenue to the district which should have, by statute, been shifted to the ERAF. In return, the ERAF was underallocated property tax revenue in the amount of the city's required population shift amount.

The Auditor-Controller is responsible for the proper allocation and apportionment of property tax revenues. The SCO believes the Auditor-Controller should not have implemented the tax exchange agreement until the city's entire ERAF obligation had been accounted for. The SCO recommends that the county act as a facilitator between the City of Placerville and El Dorado County Fire District to negotiate a plan to repay the underallocated ERAF amount.

## **Glenn County (July 1, 1997, through June 30, 2002)**

### **Follow-up on Prior Audit Findings**

Findings noted in the prior audit report, dated June 17, 1998, have been satisfactorily resolved by the county.

The audit disclosed that the county complied with California statutes for the allocation and apportionment of property tax revenues for the period audited.

## Imperial County (July 1, 1996, through June 30, 2001)

### Follow-up on Prior Audit Findings

Findings noted in the prior audit, dated October 29, 1997, have not been satisfactorily resolved by the county and are restated in this report.

### FINDING 1— Calculation and distribution of ATI

The county failed to take full corrective action for prior fiscal year errors in the AB 8 system.

In the previous two SCO audits, it was determined that the county recomputed tax rate area increment factors annually. These factors are used to compute annual revenue growth and are required by statute to remain unchanged except to accommodate changes in service responsibilities. The county's methodology computes the annual tax increment (ATI) in error and also carries forward an incorrect base revenue for each fiscal year.

The county froze the TRA factors in fiscal year (FY) 1988-89 without correcting the base revenues and jurisdictional change errors and used those frozen factors beginning in FY 1997-98.

Requirements for the apportionment and allocation of the ATI are found in *Revenue and Taxation Code* Sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to TRAs on the basis of each TRA's share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction's ATI apportionment factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

### Recommendation

The county must begin the correction by using the TRA factors that were established in FY 1979-80, adjust those factors for any jurisdictional changes, and carry forward the base revenue. This correction must be done for each fiscal year up to the current fiscal year.

### County's Response

I agree with the finding but do not feel that we can go back to 1979-80 to make the corrections. From 1979 to 1988, there was very little economic change in Imperial County. The freezing of the factors in 1988-1989 was done with the concurrence of your auditor. We will go back to that date and correct forward, because I don't feel that changes prior to that date would be material.

### SCO's Comment

The SCO is unable to determine if the adjustments will have a material impact. However, as stated above, this error was noted in the two previous SCO audits. Therefore, the county should make the corrections using the TRA factors established in FY 1979-80, adjust those factors for any jurisdictional changes, and carry forward the base revenue.

## **FINDING 2— Jurisdictional changes**

The county did not take corrective action for prior fiscal year errors in jurisdictional changes. In addition, jurisdictional changes for the current audit period were computed in error for all annexations.

In our previous two audits, it was determined that some jurisdictional change transactions were not completed as specified in their governing resolutions.

In the current audit, existing TRA base revenues were incorrectly adjusted, resulting in zero base revenue for the newly created TRAs and no adjustment to the existing TRA. The master agreement specifies that annexations with a certain level of assessed valuation at time of application will require adjustments to the base revenue.

The county computation of increment exchange resulted in changes to the fixed factors for all jurisdictions in the existing TRA and the new TRA. The master agreement specifies that increment will be exchanged only between entities with agreements. In addition, if the annexing entity assumes specific service responsibility, then the existing servicing entity must transfer 100% of all prior base and increments to the annexing entity.

The legal requirements for jurisdictional changes are found in *Revenue and Taxation Code* Section 99. A jurisdictional change involves a change in organization or boundaries of local government agencies and school districts. Normally, these are service area or responsibility changes between the local jurisdictions. As part of the jurisdictional change, the local government agencies are required to negotiate any exchange of base year property tax revenue and annual tax increment. After the jurisdictional change, the local agency whose responsibility increased receives additional ATI, and the base property tax revenues are adjusted according to the negotiated agreements.

### Recommendation

The county must review all jurisdictional changes and correct the TRA factors and base revenues for all entities impacted.

### County's Response

I agree with the finding and we are currently gathering the data necessary to begin the calculations. Given our current budget crisis in the county and my shortage of staff I anticipate this will take several months. At some point we will probably be contacting your office for assistance in the proper methods to use.

## **FINDING 3— Supplemental property tax**

The county did not take corrective action for prior fiscal years' noncompliance to apportion supplemental tax twice annually as required by statute. In addition, the current process is not in compliance as follows:

- The county included the RDA in the calculation of supplemental apportionment factors; and
- The county included the ERAF in the average daily attendance (ADA) total revenue calculation.

The legal requirements for supplemental roll property tax apportionment and allocation are found in *Revenue and Taxation Code* Sections 75.60 through 75.71 and 100.2. When there is a change in assessed property value due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

#### Recommendation

The county must apportion the supplemental revenue twice annually as required by the statute. In addition, the RDA increment must be apportioned directly to the RDA, and the ERAF must be excluded from the ADA recomputation.

#### County's Response

We agree with the findings have met with the Tax Collector and will apportioning [sic] as required beginning this fiscal year.

### **FINDING 4— Supplemental property tax— administrative costs**

The county did not take corrective action for prior fiscal years' noncompliance to document and identify the supplemental administration costs.

*Revenue and Taxation Code* Section 75.60 allows a county to charge an administrative fee for supplemental property tax collections. This fee is not to exceed 5% of the supplemental property taxes collected.

#### Recommendation

The county must identify and document the supplemental administration costs in order to qualify for the 5% administrative cost reimbursement.

#### County's Response

We agree with the finding and will comply, as soon as we have verified that all proper documentation is available and correct. We will then perform this task as required.

### **FINDING 5— Redevelopment agencies**

The county did not take full corrective action for prior fiscal year errors in the RDA base assessed values. RDAs established prior to 1990 did not include assessed values for unsecured and homeowner property tax relief (Hopter). RDAs established after 1990 include Hopter but exclude assessed unsecured values.

Requirements for the apportionment and allocation of property tax to RDAs are found in *Revenue and Taxation Code* Sections 96.4 and 96.5. California Community Redevelopment Law generally entitles a community redevelopment agency to all of the property tax revenues that are realized from growth in values since the redevelopment project's inception.

Recommendation

The county must correct all the base assessed values for all the RDAs.

County's Response

Will be corrected when Finding 2 has been completed.

**FINDING 6—  
Unitary and  
operating nonunitary  
apportionment**

The county incorrectly computed the unitary and operating nonunitary apportionment and debt service rate as follows:

- The county did not include the ERAF and certain RDAs in the unitary apportionment;
- The county excluded the pipeline assessed valuation from the unitary assessed valuation; and
- The county did not use the ad valorem debt service levy for the secured roll to compute the unitary debt service rate.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in *Revenue and Taxation Code* Section 100.

Unitary properties are those properties on which the Board of Equalization “may apply the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee” (i.e., public utilities and railroads). The *Revenue and Taxation Code* further states, “Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee.”

In FY 1988-89, the Legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The unitary and operating nonunitary base year was established and formulas were developed to compute the distribution factors for the fiscal years that followed.

Recommendation

The following revisions must be made to the county unitary system:

- All jurisdictions must be included in the unitary process;
- The pipeline assessed valuation assessed by the county assessor must be included in the total unitary assessed valuation; and
- The county must use the ad valorem service levy for the secured roll to compute the unitary debt service rate.

County's Response

Was discussed and corrected during the audit.

**FINDING 7—  
Educational Revenue  
Augmentation Fund  
(ERAF)**

The county did not take full corrective action for prior fiscal year errors in the ERAF shift. For the current audit period, the county incorrectly computed the ERAF revenue. The errors are as follows:

- The ERAF shift from FY 1992-93 through FY 2001-02 was computed using incorrect AB 8 apportionment factors (see Finding 1).
- From FY 1995-96 through FY 2001-02, the county apportioned a total of \$225,282 of ERAF revenue to the El Centro RDA.
- ERAF was excluded from the unitary and operating non-unitary apportionment process (Schedule 1).

Requirements for the local agency shift of property tax revenues to the ERAF are generally found in *Revenue and Taxation Code* Sections 97.1 through 97.3. Beginning in FY 1992-93, each local agency was generally required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF are subsequently allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was generally determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was generally determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts was generally determined by shifting the lesser of 10% of that district's total annual revenues as shown in the FY 1989-90 edition of the State Controller's *Report on Financial Transactions Concerning Special Districts* or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties was generally determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, was generally determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting this amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting this amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding this amount to the FY 1992-93 ERAF shift, adjusting for growth.



For fire districts, the FY 1993-94 ERAF shift was generally determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;
- Adjusting this amount for growth; and
- Adding this amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years subsequent to FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

#### Recommendation

The county must recompute the ERAF shift using correct AB 8 factors, correct the unitary and operating nonunitary apportionment process, and retroactively correct the ERAF revenue.

#### County's Response

This will be corrected when the recalculations of Finding 2 have been implemented. I believe that the retroactivity issue is covered under AB169, and therefore we will not retroactive collect the apportionment from the RDA. We have corrected the apportionment to the RDA for this current year and will continue to apportion correctly in the future.

#### SCO's Comment

After the county recomputes the AB 8 factors and corrects the unitary and operating nonunitary apportionment process, the county should determine if the retroactivity is covered under AB 169. If not, then the county should retroactively correct the ERAF revenue.

## **Kern County (July 1, 1998, through June 30, 2001)**

### **Follow-up on Prior Audit Findings**

Findings noted in the prior audit report, dated June 30, 1999, have been satisfactorily resolved by the county.

### **FINDING— Redevelopment agencies**

The county incorrectly computed and diverted a pass-through revenue amount for the ERAF for redevelopment projects under the provisions of *Health and Safety Code* Section 33607.5. The code section provides for the pass-through of a portion of redevelopment increment to all affected

taxing agencies. However, it has been determined that the ERAF does not meet the definition of an affected taxing agency.

Requirements for the apportionment and allocation of property tax to RDAs are found in *Revenue and Taxation Code* Sections 96.4 and 96.5. California Community Redevelopment Law generally entitles a community redevelopment agency to all of the property tax revenues that are realized from growth in values since the redevelopment project's inception.

### Recommendation

The county should compute and pay to affected taxing agencies any revenues for the audit period that were improperly distributed to the ERAF.

### County's Response

Your audit finding states "the county made an error in computing redevelopment pass-through revenue." The computation of pass-through revenue was correct (20% of gross revenue). If, as the State Controller has determined, ERAF is not to be included in the allocation of pass-through revenue, then our pass-through allocation factors were incorrect because they included ERAF.

The audit report recommendation incorrectly directs the payment back to the RDA. An appropriate recommendation would be to re-distribute the ERAF portion to the other affected jurisdictions.

### Auditor's Comment

The SCO does not agree with the characterization of the audit finding. The county has included a quote from the summary and conclusion in the body of the audit report. The finding states the error correctly. The SCO would concur that the summary and conclusion should have been more specific in characterizing the error as an error in computing the pass-through revenue to affected taxing agencies.

The SCO concurs that the recommendation should state the payback should go to the other taxing agencies and has modified the recommendation accordingly.

## **Kings County (July 1, 1997, through June 30, 2002)**

### **Follow-up on Prior Audit Findings**

Findings noted in the prior audit, dated May 28, 2003, have been satisfactorily resolved by the county, with the exception of:

- The county failed to take full corrective action for prior fiscal year errors in the AB 8 apportionment system and the unitary and operating nonunitary apportionment system.
- Documentation was unavailable to support the county computation of the 1979-80 base year apportionment and tax increment. In addition, the county recomputed its ATI factors in each TRA annually. In FY 1995-96, the county froze all TRA factors but no corrections were made to the other errors.

- The county incorrectly computed the unitary and operating nonunitary base year apportionment factor by using AB 8 factors. In addition, when unitary and operating nonunitary assessed value increased by more than 102% from one year to the next, the county incorrectly computed new unitary apportionment factors.

Due to the absence of documents necessary to make the above corrections, the county should seek legislative validation for its AB 8 process and its unitary and operating nonunitary systems, beginning with FY 1995-96.

#### County's Response

The audit continues to recommend we seek legislative validation for historical errors. We do not think that is necessary nor desirable at this point.

#### SCO's Comment

The SCO does not concur with the county's position that legislative validation of historical errors is neither necessary nor desirable at this point. While many of the county's allocation and apportionment processes are correct, the county is applying these processes to incorrect property tax base amounts. Thus, property tax revenues allocated and apportioned to taxing agencies are also incorrect. The county should seek legislative validation for the current property tax amounts to preclude possible legal consequences from local taxing agencies.

### **FINDING 1— Calculation and distribution of ATI**

As stated in the prior audit, the county adjusts the current year revenue in the AB 8 system for jurisdictional change rather than the base revenue.

Requirements for the apportionment and allocation of ATI are found in *Revenue and Taxation Code* Sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to TRAs on the basis of each TRA's share of the incremental growth in assessed valuations. The ATI is then multiplied by the jurisdiction's ATI apportionment factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The ATI is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

#### Recommendation

The county should modify the AB 8 system to adjust the base revenue for jurisdictional change rather than the current revenue.

#### County's Response

The recommendation is being implemented for the 2003-4 fiscal year. The dollar amount of jurisdictional changes in Kings County is insignificant [sic].

**FINDING 2—  
Supplemental  
property tax**

As stated in the prior audit, the county apportioned supplemental revenues to the RDAs using the supplemental apportionment factors.

The legal requirements for supplemental roll property tax apportionment and allocation are found in *Revenue and Taxation Code* Sections 75.60 through 75.71 and 100.2. When there is a change in assessed property value due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

**Recommendation**

The county must remove the RDAs from the supplemental apportionment system. Supplemental revenues collected within the RDA projects should be allocated directly to the projects.

**County's Response**

The recommendation is being implemented for the 2003-4 fiscal year.

**FINDING 3 —  
Redevelopment  
agencies**

As stated in the prior audit, the RDAs within the county report summaries of "Statement of Indebtedness" rather than by projects.

Requirements for the apportionment and allocation of property tax to RDAs are found in *Revenue and Taxation Code* Sections 96.4 and 96.5. California Community Redevelopment Law generally entitles a community redevelopment agency to all of the property tax revenues that are realized from growth in values since the redevelopment project's inception.

**Recommendation**

During SCO fieldwork, the county implemented a corrective action to remedy this issue.

**County's Response**

As noted this recommendation has been corrected.

**Los Angeles County (July 1, 1999, through June 30, 2001)****Follow-up on Prior  
Audit Findings**

The county had not satisfactorily resolved the findings noted in the prior audit report, dated May 31, 2001. One of the findings is restated in this audit report, and the other was resolved through litigation, also noted in this audit report.

**FINDING 1 —  
Redevelopment agencies**

The county has had a continuing problem identifying all unsecured parcels within redevelopment agency (RDA) tax rate areas (TRAs) and transferring them to new TRAs created when an RDA is established.

Previous audit reports have noted that parcels with unsecured value that were located within the boundaries of an RDA have often been assigned to TRAs outside of the RDA. This incorrect assignment of unsecured value has resulted in an understatement of revenues due to the RDA from the unsecured roll. Based on discussions with the staff in the County Assessor's Office and the County Auditor-Controller's Office, these corrections should be handled in the County Assessor's Office.

The current audit found that the county also has a problem identifying all secured parcels within RDA TRAs and transferring them to new TRAs created when an RDA is established.

Requirements for the apportionment and allocation of property tax to RDAs are found in *Revenue and Taxation Code* Sections 96.4 and 96.5. California Community Redevelopment Law generally entitles a community RDA to all of the property tax revenues that are realized from growth in values since the redevelopment project's inception.

#### Recommendation

The county should review the recently developed procedures and install appropriate safeguards to ensure that all unsecured and secured parcels within RDA project boundaries are properly identified and recorded in new TRAs.

#### County's Response

We agree. The Assessor's [sic] Systems Division will develop a program to ensure that secured and unsecured parcels within RDA project boundaries are properly identified and recorded in new tax rate areas.

The Assessor's Office has been notified of the RDA parcels assigned to incorrect tax rate areas. These occurrences cited by your staff will be corrected in fiscal year 2003-04 since the Assessor's Roll for FY 2002-03 has been closed.

## **FINDING 2— Educational Revenue Augmentation Fund (ERAF)**

The prior audit found that the county properly reversed the ERAF disaster relief revenue for all appropriate cities and the county's General Fund, but did not make corresponding adjustments to TRA factors to correct the growth portion of this adjustment. During the current audit period (fiscal year (FY) 1999-2000 through FY 2000-01) the county again did not make the required adjustments to the TRA factors. However, in FY 2001-02 the county did make the required adjustments to the TRA factors, with the exception of the City of Santa Clarita. The dollar amount was determined to not be material.

The following finding was adjudicated by the courts and therefore has been withdrawn.

The county properly computed a reversal of the Consolidated Fire District ERAF contribution for FY 1992-93, but adjusted only the base revenue for the district and did not compute and transfer revenue retroactively, as required by AB 1589 (Chapter 290, Statutes of 1997). The county also failed to adjust the FY 1993-94 ERAF computation for

the fire district to reflect the revenue adjustment for FY 1992-93. In a subsequent lawsuit between the Consolidated Fire District, Los Angeles County, and the State of California, it was determined that the Fire District was entitled to a refund of excess ERAF contributions from past years and that the refund from ERAF in future years must be corrected. Details of the adjustments are shown on Schedule 1, "Summary of Overallocation to the Educational Revenue Augmentation Fund."

Requirements for the local agency shift of property tax revenues to the ERAF are generally found in *Revenue and Taxation Code* Sections 97.1 through 97.3. Beginning in FY 1992-93, each local agency was generally required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF are subsequently allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was generally determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was generally determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts was generally determined by shifting the lesser of 10% of that district's total annual revenues, as shown in the FY 1989-90 edition of the State Controller's *Report on Financial Transactions Concerning Special Districts*, or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties was generally determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, was generally determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting this amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting this amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding this amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift was generally determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;
- Adjusting this amount for growth; and
- Adding this amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years subsequent to FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

The following schedule summarizes the overallocation to the ERAF by fiscal year.

<u>Fiscal Year</u>	<u>Allocation by County</u>	<u>County Corrected Amount per Audit<sup>1</sup></u>	<u>Audit Adjustment</u>
1992-93	\$ 19,515,603	\$ —	\$ (19,515,603)
1993-94	11,763,560	(11,899,312)	(23,662,872)
1994-95	11,999,909	(11,928,400)	(23,928,309)
1995-96	11,892,174	(11,957,728)	(23,849,902)
1996-97	11,878,488	(11,987,300)	(23,865,788)
1997-98	(8,389,836)	(12,017,117)	(3,627,281)
1998-99	(8,389,836)	(12,047,181)	(3,657,345)
1999-2000	(8,389,836)	(12,077,494)	(3,687,658)
2000-01	(8,389,836)	(12,108,058)	(3,718,222)
2001-02	(8,389,836)	(12,138,876)	(3,749,040)
2002-03	(8,389,836)	(12,169,949)	(3,780,113)
Totals	\$ 16,710,718	\$ (120,331,415)	\$ (137,042,133)

<sup>1</sup> Agreed to by the State Controller's Office.

### Recommendation 1

Although the county has corrected all of the TRA factors except for the City of Santa Clarita, the corrections were made outside of the scope of the current audit period. The county should correct the TRA factor for the City of Santa Clarita, so that the full correction can be validated in the next audit.

### County's Response to Recommendation 1

We agree. The City of Santa Clarita TRA factor will be corrected in fiscal year 2002-03 during the Apportionment Processing.

### Recommendation 2

In response to the lawsuit, this recommendation replaces the original recommendation.

The county has computed the total amount of ERAF refund due to the fire district through FY 2002-03 and has received concurrence with the computations by the fire district and the State of California. That amount should be refunded to the district and the ERAF amount for the subsequent years should be computed as agreed upon by all parties and confirmed by the Superior Court of Los Angeles. The following reply by the county was written in response to the original finding.

### County's Response to Recommendation 2

We disagree.

The State Controller's Office (SCO) recently has completed an audit, pursuant to Government Code Section 12468, of the methods employed by Los Angeles County to apportion and allocate property tax revenues for the period of July 1, 1999, through June 30, 2001. The SCO's draft audit report states, among other things, that:

"The county had not satisfactorily resolved the findings noted in the prior audit report, dated May 31, 2001"

As the draft audit report confirms, the finding referred to above is concerned with the calculation method prescribed by Revenue and Taxation Code section 97.3(c), commonly known as the 93/94 ERAF Shift.

The County of Los Angeles and the Consolidated Fire Protection District of Los Angeles County challenged the findings of the prior audit report dated May 31, 2001 as plaintiffs and petitioners against State Controller Kathleen Connell and the State of California in an action filed April, 2002 in Los Angeles Superior Court, styled "CONSOLIDATED FIRE PROTECTION DISTRICT OF LOS ANGELES COUNTY, et al., v. KATHLEEN CONNELL, etc., et al., Case No. BS 075435. The County and District sought a writ of mandate commanding the Controller to revise her May 2001 audit report and February 2002 report to the State Legislature so the findings in those reports which pertain to the impact of the 93-94 ERAF Shift on the Fire District are in accordance with the calculation method prescribed by Revenue and Taxation Code section 97.3(c). Specifically, that the audit findings be revised to reflect that the proper calculation of the 93/94 ERAF Shift be based upon the actual historical property tax figures for the 1992-1993 fiscal year. Plaintiffs and petitioners also sought declaratory relief to the same effect against defendant Connell and the State of California.

On July 11, 2002 in Department 85 of the above referenced court, the Honorable Dzintra Janavs granted plaintiff/petitioners' Motion for Issuance of a Peremptory Writ of Mandate. The Court's tentative decision was ordered filed as its written Statement of Decision, a copy of which is enclosed with this response.



Furthermore, on August 7, 2002 the Court granted plaintiff/petitioners' Motion for Summary Adjudication upon their claim for Declaratory Relief as against the Controller and the State of California. Significantly, one of the bases for the Court's declaratory relief ruling was a recognition that audits would recur in the future, and it was appropriate to issue comprehensive declaratory relief to ensure that, in future audits, the Controller would not adhere to the erroneous interpretation of the 93/94 Shift reflected in the May 31, 2001 audit report. Here, too, the court ordered filed its written statement of decision, a copy of which is enclosed with this response.

Collectively, these rulings establish two points with respect to allocation of property taxes in light of AB 1589, enacted in 1997: (i) in light of AB 1589, the District is entitled to a refund of all monies paid under Revenue and Taxation Code section 97.2, a separate statute commonly known as the 92/93 ERAF Shift; and (ii) despite AB 1589, the separate 93/94 ERAF Shift is to remain unchanged, and is based upon actual historical figures for the 1992-1993 fiscal year. Both the May 31, 2001 prior audit and the current audit correctly recognize that the District is entitled to a refund of all monies paid under the 92/93 ERAF Shift, but incorrectly assert that the County's calculation of the 93/94 Shift is wrong, even though the County's interpretation has been endorsed, and the SCO's interpretation rejected, by the Court.

Based upon the foregoing, the Los Angeles County Auditor-Controller requests that the draft audit finding stated above should be removed from the final report, and the report modified to comport with the Court's rulings. (Of course, as ordered by the Court, the May 31, 2001 audit report and the February 2002 report to the Legislature should be modified as well.) Under no circumstances should the audit report include a "finding" which has been ordered corrected by the Court.

#### SCO's Comment

As stated above, this finding was adjudicated by the courts and therefore has been withdrawn.

## **Mendocino County (July 1, 1996, through June 30, 2001)**

### **Follow-up on Prior Audit Findings**

Findings noted in the prior audit, dated December 31, 1997, have not been satisfactorily resolved by the county, and are being restated in this report.

### **FINDING 1— Calculation and distribution of ATI**

The county did not correct prior errors in the AB 8 system. In FY 1997-98, the county froze the TRA factors but did not correct the prior-year base revenues and TRA factors for the following errors:

- The county recomputed the annual tax increment (ATI) TRA factors annually up to FY 1996-97;
- The annual recomputation up to FY 1993-94 included a Special District Augmentation Fund (SDAF) revenue adjustment in the TRA factors; and
- The unitary and operating nonunitary base revenue, computed in FY 1987-88, was included in the AB 8 process up to FY 1996-97.

Requirements for the apportionment and allocation of the ATI are found in *Revenue and Taxation Code* Sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to TRAs on the basis of each TRA's share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction's ATI factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

### Recommendation

The county must correct the above errors and recompute the base revenues and TRA factors from FY 1978-79 to present. The county should implement procedures so that errors in the property tax system are corrected in a timely manner and in conformance with the *Revenue and Taxation Code*.

### County's Response

We reiterate our position from the prior audit report comments that the county did not err in re-computing the annual tax increment. Our approach was based upon your approved 1987 audit findings and recommendations. We further believe that the County of Mendocino is in compliance with state statute on a prospective basis commencing in fiscal year 1997-98.

### SCO's Comment

The SCO reiterates its position from the previous audit. The fact remains that the county did not comply with the provisions of the *Revenue and Taxation Code*. The county has the ultimate responsibility to ensure that the allocation and apportionment of property tax revenues are in accordance with statutory requirements. The statutes require that ATI factors remain constant except for the effects of jurisdictional changes. The finding remains as written.

## **FINDING 2— Jurisdictional changes**

The county failed to correct jurisdictional change errors identified in the previous SCO audit. In that audit, the SCO noted, "The county does not include TRA factor exchange negotiations in the jurisdictional exchange process." The county continues to process jurisdictional changes in the same manner.

The legal requirements for jurisdictional changes are found in *Revenue and Taxation Code* Section 99. A jurisdictional change involves a change in organization or boundaries of local government agencies and school districts. Normally, these are service area or responsibility changes between the local jurisdictions. As part of the jurisdictional change, the local government agencies are required to negotiate any exchange of base-year property tax revenue and ATI. After the jurisdictional change, the local agency whose responsibility increased receives additional ATI, and the base property tax revenues are adjusted according to the negotiated agreements.

Recommendation

The county must review all jurisdictional changes and correct the TRA factors of jurisdictions that were inappropriately changed. These corrections must be completed in conjunction with the corrections recommended in Finding 1. The county should implement procedures so that errors in the property tax system are corrected in a timely manner and in conformance with the *Revenue and Taxation Code*.

County's Response

We reiterate our position from the prior audit report comments that the county did not err in re-computing the annual tax factors. Our approach was based upon your approved 1987 audit findings and recommendations. We further believe that the County of Mendocino is in compliance with state statute on a prospective basis commencing in fiscal year 1997-98.

SCO's Comment

The SCO reiterates its position from the previous audit. The fact remains that the county did not comply with the provisions of the *Revenue and Taxation Code*. The county has the ultimate responsibility to ensure that the allocation and apportionment of property tax revenues are in accordance with statutory requirements. The statutes require that ATI factors remain constant except for the effects of jurisdictional changes. The methodology used by the county changes all ATI factors annually, regardless of whether or not an entity was party to a jurisdictional change. The finding remains as written.

**FINDING 3—  
Supplemental  
property tax—  
administrative costs**

The county failed to correct a prior audit finding in identifying costs associated with the supplemental property tax administrative cost reimbursement. The county documented the auditor-controller's accountant salary but excluded all other costs. As a result, the FY 2000-01 first allocation reimbursement exceeded 5% of collected revenue.

*Revenue and Taxation Code* Section 75.60 allows a county to charge an administrative fee for supplemental property tax collections. This fee is not to exceed 5% of the supplemental property taxes collected.

Recommendation

The county should document and identify all costs associated with administering the supplemental property tax revenues. The county should implement procedures so that errors in the property tax system are corrected in a timely manner and in conformance with the *Revenue and Taxation Code*.

County's Response

We concur with your findings and have implemented a process which will insure full documentation of all costs associated with administering the supplemental property tax revenue program in a more timely manner.

**FINDING 4—  
Unitary and operating  
nonunitary  
apportionment**

The county failed to correct prior errors in the unitary and operating nonunitary apportionment factors. The base revenue and apportionment factors were corrected, but no adjustment was made for fiscal years when revenue exceeded 102%.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in *Revenue and Taxation Code* Section 100.

Unitary properties are those properties on which the Board of Equalization “may apply the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee” (i.e., public utilities and railroads). The *Revenue and Taxation Code* further states, “Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee.”

In FY 1988-89, the Legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The unitary and operating nonunitary base year was established and formulas were developed to compute the distribution factors for the fiscal years that followed.

Recommendation

The county must adjust the base revenue for all fiscal years when revenue exceeded 102%. This correction must be completed in conjunction with the corrections recommended in Finding 1. The county should implement procedures so that errors in the property tax system are corrected in a timely manner and in conformance with the *Revenue and Taxation Code*.

County’s Response

We reiterate our position from the prior audit report comments that the county did not err in re-computing the annual tax factors. Our approach was based upon your approved 1987 audit findings and recommendations. We further believe that the County of Mendocino is in compliance with state statute on a prospective basis commencing in fiscal year 1997-98.

SCO’s Comment

The SCO reiterates its position from the previous audit. The fact remains that the county did not comply with the provisions of the *Revenue and Taxation Code*. The county has the ultimate responsibility to ensure that allocation and apportionment of property tax revenues are in accordance with statutory requirements. The prior audit covered a period ending with FY 1986-87. The base year for the unitary and operating nonunitary system is FY 1987-88. This was after the last audit period and, consequently, was not covered by that audit. The county used an inappropriate methodology to develop the base amounts for the unitary and operating nonunitary system. Rather than developing factors based upon the proportionate share of unitary and operating nonunitary revenue

received by local jurisdictions, the county inappropriately applied a countywide AB 8 factor. In addition, when the Legislature abolished the SDAF in FY 1993-94, the county inappropriately distributed the SDAF factor within the unitary and operating nonunitary system to the county general fund and cities in the county rather than solely to the entities that had made SDAF contributions in the development of the SDAF factor. The finding remains as written.

**FINDING 5 —  
Property tax  
administrative costs**

The county incorrectly computed the eligible cost for the Assessor's Office by including 100% of costs rather than the 50% eligible.

Requirements for the reimbursement of county property tax administrative costs are found in *Revenue and Taxation Code* Section 95.3. County property tax administrative costs are incurred by the assessor, the tax collector, the assessment appeals board, and the auditor. The county is allowed, depending on the fiscal year and any corresponding exclusions, to be reimbursed by local agencies and public schools for these administrative costs.

Recommendation

The county should include only eligible costs associated with administering the property tax system to compute the administrative cost reimbursement. The county should implement procedures to review the costs so errors are identified.

County's Response

We concur with your findings and have implemented a process, which will include only eligible costs associated with administering the property tax system to compute the administrative cost reimbursement.

**FINDING 6—  
Educational Revenue  
Augmentation Fund  
(ERAF)**

The county failed to take full corrective action for prior errors in the ERAF shift. The prior fiscal year ERAF shift included the following errors:

- The FY 1992-93 ERAF (9% of revenue) computation for one city was overstated because the prior revenue amount used was different from the city revenue amount used in the prior-year AB 8 reports.
- The FY 1993-94 special district ERAF computations did not include the SDAF participation adjustment required.
- The county included the ERAF in the TRA factor recomputation each fiscal year up to FY 1996-97. Recomputing the TRA factors annually causes the growth share of the ERAF to be shared by all jurisdictions, rather than just the local agencies that are required to contribute to the ERAF.

For the current SCO audit, in FY 1997-98 the county did not reverse the disaster relief amount of \$32,467 from the cities and the county to the ERAF.

As the errors encompass numerous fiscal years and many complex computations, the SCO auditor was unable to determine and report the total error in the ERAF shift.

Requirements for the local agency shift of property tax revenues to the ERAF are generally found in *Revenue and Taxation Code* Sections 97.1 through 97.3. Beginning in FY 1992-93, each local agency was generally required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF are subsequently allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was generally determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was generally determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts was generally determined by shifting the lesser of 10% of that district's total annual revenues as shown in the FY 1989-90 edition of the State Controller's *Report on Financial Transactions Concerning Special Districts* or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties was generally determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, was generally determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the SDAF factor for the district effective on June 15, 1993;
- Adjusting this amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting this amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding this amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift was generally determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net

current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;

- Adjusting this amount for growth; and
- Adding this amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years subsequent to FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

#### Recommendation

The ERAF shift amount must be corrected in conjunction with all the other findings in this report. Once the shift amount has been corrected, the ERAF revenue must be adjusted accordingly. The county should implement procedures so that errors in the property tax system are corrected in a timely manner and in conformance with the *Revenue and Taxation Code*.

#### County's Response

We reiterate our position from the prior audit report comments that the county did not err in re-computing the appropriate ERAF amount. Our approach was based upon your approved 1987 audit findings and recommendations. We further believe that the County of Mendocino is in compliance with state statute on a prospective basis commencing in fiscal year 1997-98.

Regarding the comments made relative to the reversal of the disaster relief amount of \$32,467, we wish to point out that the counties' share of \$15,644 was in fact reversed in fiscal year 1997-1998 but was overlooked by your auditor. The remaining balance pertaining to the cities' portion of \$16,823 was reversed earlier this fiscal year.

#### SCO's Comment

As stated in Finding 1, the SCO reiterates the position that it was inappropriate to recalculate apportionment factors, including ERAF apportionment factors. The SCO acknowledges the county's disaster relief amount was reversed. However, when the county froze the factors, the disaster relief amount was inadvertently omitted from the computation.

## Mono County (July 1, 1997, through June 30, 2002)

### Follow-up on Prior Audit Findings

Findings noted in the prior audit report, dated July 21, 1997, have been satisfactorily resolved by the county.

### FINDING 1— Property tax administrative costs

The county failed to properly capture all supplemental administrative costs collected for inclusion with revenues collected to offset the computation of county-wide administrative costs. This oversight resulted in an overstatement of administrative costs that were charged to local agencies each year.

Requirements for the reimbursement of county property tax administrative costs are found in *Revenue and Taxation Code* Section 95.3. County property tax administrative costs are incurred by the assessor, the tax collector, the assessment appeals board, and the auditor. The county is allowed, depending on the fiscal year and any corresponding exclusions, to be reimbursed by local agencies and public schools for these administrative costs.

#### Recommendation

During the fieldwork portion of this audit, the county computed the total supplemental administration amounts that had been excluded in the prior years and made an adjustment to the county-wide administrative costs for FY 2002-03. The county provided a copy of the proposed correction to the SCO auditor, to be implemented at the close of the FY 2002-03 property tax process. The adjustment amount computed should properly correct this issue.

This item will be reviewed during the next audit to confirm that the correction was properly implemented. No further action will be required.

### FINDING 2— Educational Revenue Augmentation Fund (ERAF)

The county properly computed ERAF per capita amounts for the county and city at the close of the prior audit. When those computations were carried forward to this audit period, the per capita amounts had been deleted, resulting in an understatement of ERAF contributions for all years of this audit.

Requirements for the local agency shift of property tax revenues to the ERAF are generally found in *Revenue and Taxation Code* Sections 97.1 through 97.3. Beginning in FY 1992-93, each local agency was generally required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF are subsequently allocated to public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was generally determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was generally determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts was generally determined by shifting the lesser of 10% of that district's total annual revenues, as shown in the FY 1989-90 edition of the State Controller's *Report on*



*Financial Transactions Concerning Special Districts*, or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties was generally determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, was generally determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting this amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting this amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding this amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift was generally determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;
- Adjusting this amount for growth; and
- Adding this amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years subsequent to FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

#### Recommendation

Prior to the conclusion of fieldwork portion of this audit, the county computed the amount of the per capita understatement for the county and

city for all years with growth. A copy of the county spreadsheet was provided to the SCO auditor, and the county proposed to transfer the total to the ERAF and make an adjustment to the year-end revenues for FY 2002-03 to correct this issue. The amounts computed would properly correct the total amount underpaid for this audit period, and the per capita amounts would then be correct.

This item will be reviewed during the next audit to confirm that the correction was properly implemented. No further action will be required.

## Nevada County (July 1, 1997, through June 30, 2002)

### Follow-up on Prior Audit Findings

Findings noted in the prior audit report, dated October 28, 1998, have been satisfactorily resolved by the county.

### FINDING 1— Calculation and distribution of ATI

The county reduced the amount computed for the ERAF in FY 2000-01 to the prior year amount in anticipation of a permanent reduction that had been proposed for that year. When the reduction did not materialize, the county failed to correct its earlier computation, which understated the ERAF and total amount to apportion. This resulted in an underpayment to the ERAF of \$593,840, with a corresponding overpayment to local agencies of \$275,928; to K-12 Schools of \$245,156; to Community Colleges of \$57,701; to Superintendent of Schools of \$5,869; and to other school programs of \$9,186.

Requirements for the apportionment and allocation of the annual tax increment (ATI) are found in *Revenue and Taxation Code* Sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to TRAs on the basis of each TRA's share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction's ATI factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

### Recommendation

The amounts overpaid to all local agencies, but not schools or school entities, must be computed, collected, and paid to the ERAF. Since some of the overpayment went to schools, it would not be productive to refund revenue from the schools to the ERAF and then return it to the schools.

### County's Response

**Response:** The Fiscal Year 2000/2001's ERAF amount was the same as the 1999/2000 Fiscal Year's amount. We found R&T Code #97.43 which stated the FY99/00 ERAF amount can be used as a ceiling for future fiscal year ERAF amounts. During the audit, the State Auditor researched this R&T Code and he stated that the Code is valid, but the conditions below the Code made it unusable. Thus, we need to reportion the variance.

**Action:** The corrections will be made and the variance will be reapportioned in FY 2003/04.

## **FINDING 2— Jurisdictional changes**

The county properly computed all revenue exchanges between jurisdictions for FY 2000-01 and FY 2001-02, but when these amounts were carried forward to the AB 8 process to adjust base revenue for the jurisdictions involved, the amounts computed were brought forward in error. This error resulted in some jurisdictions receiving slightly more revenue than they were entitled to, while some others received slightly less. None of these errors were significant, but since they involved revenue amounts that are carried forward to future years, corrections must be made.

The legal requirements for jurisdictional changes are found in *Revenue and Taxation Code* Section 99. A jurisdictional change involves a change in organization or boundaries of local government agencies and school districts. Normally, these are service area or responsibility changes between the local jurisdictions. As part of the jurisdictional change, the local government agencies are required to negotiate any exchange of base year property tax revenue and annual tax increment. After the jurisdictional change, the local agency whose responsibility increased receives additional annual tax increment, and the base property tax revenues are adjusted according to the negotiated agreements.

### Recommendation

Appropriate adjustments must be made to the base revenue amounts for all affected jurisdictions.

### County's Response

**Response:** The correct calculated amounts of growth on the annexations were not transferred onto the AB8 spreadsheet.

**Action:** The State Auditor's correction worksheet has been added to the current FY03/04 base year adjustments and has been included on the AB8 spreadsheet.

## **FINDING 3— Supplemental property tax**

The county uses AB 8 factors that include redevelopment agencies to compute supplemental property tax revenue. This is contrary to *Revenue and Taxation Code* Section 75.70(c)(1), which requires that redevelopment increment be computed and paid "off the top" only. The rest of the supplemental factor computations were correct, except that when a sample apportionment was tested for FY 2000-01 and FY 2001-02, the factors computed by the county were not used by the data processing system. No measurable impact was noted on any one jurisdiction as a result of this error.

The legal requirements for supplemental roll property tax apportionment and allocation are found in *Revenue and Taxation Code* Sections 75.60 through 75.71 and 100.2. When there is a change in assessed property value due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

Recommendation

The misallocations resulting from the above errors were determined to be immaterial, but the supplemental property tax factor computation procedure must be corrected for all future year computations.

County's Response

**Response:** A. The programmer assigned to our department from Information Services and our staff have researched the questioned apportionment factors. We found that the Supp system apportions the receipts, it divides the apportionment by fiscal years, then the program uses that year's AB8 factors to apportion that year's receipts. The report the State Auditor was auditing is a summary by Fund numbers of this program; it does not have the detail by fiscal year and the year's apportionment factors.

B. As directed by the State Auditor, we have corrected the Supplemental apportionment of the County's RDA's in the FY 2003/04.

**Action:** A. No further work is needed. The apportionment process is correctly distributing taxes.

B. We have deleted the RDA's factors from the Supplemental AB8 percentages as directed. Also, we are distributing a 100% of the taxes in RDA TRAs to the RDA Districts.

**FINDING 4 —  
Redevelopment  
agencies**

The base year values used for the computation of increment for the Town of Truckee redevelopment project were incorrect. The county used the FY 1999-2000 values, but should have used values for FY 1998-99.

Requirements for the apportionment and allocation of property tax to RDAs are found in *Revenue and Taxation Code* Sections 96.4 and 96.5. California Community Redevelopment Law generally entitles a community redevelopment agency to all of the property tax revenues that are realized from growth in values since the redevelopment project's inception.

Recommendation

The county was aware of this problem and had already begun to gather the correct year values. Since the correct values had not been completed before this audit was completed, the county is urged to continue the correction process and compute corrected increment amounts for this audit period and make appropriate adjustments to all affected jurisdictions.

County's Response

**Response:** We were using the FY 1999/00 for the Base Year due to the RDA not being enrolled by the Board of Equalization in the year indicated by the RDA's Statement of Incorporation. During the FY 2002/03, County Counsel gave our office a letter indicating that the Base Year was to be FY 1998/99.

**Action:** We have worked with the Assessor's Office and we have the FY98/99's Base Years A.V. values, we also have the revised A.V. values for the FY 2000/2001, 2001/2002, 2002/2003. Our office has revised the RDA calculations for FY 2000/2001-2003/2004. All of this information has been sent to the Truckee RDA.

**FINDING 5—  
Unitary and operating  
nonunitary  
apportionment**

The county failed to properly compute unitary and operating nonunitary apportionment factors for FY 1997-98 when the revenue increased over the prior year by more than 2%. Due to this error, all jurisdictions received the incorrect amount of unitary property taxes for all years addressed by this audit. While some jurisdictions were overpaid for this period, most notably the County General fund by \$109,983, many others were underpaid, most notably the ERAF by \$91,755 and the Town of Truckee by \$28,285.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in *Revenue and Taxation Code* Section 100.

Unitary properties are those properties on which the Board of Equalization "may apply the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities and railroads). The *Revenue and Taxation Code* further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the Legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The unitary and operating nonunitary base year was established and formulas were developed to compute the distribution factors for the fiscal years that followed.

**Recommendation**

The overpayments and underpayments to all jurisdictions for this audit period must be corrected and appropriate revenue transfers completed, and the unitary and operating nonunitary base revenue must be corrected to carry forward to future years.

**County's Response**

**Response:** We were using Revenue and Taxation Code #98 to apportion the taxes. During the audit, we were informed that R&T Code #98 has been repealed [sic] and we should have been using Section 100. Due to this error we have apportioned the Unitary Taxes incorrectly. The State Auditor created a worksheet of the corrections that we will use to correct this finding.

**Action:** We will use the State Auditor's worksheet to make the adjustment in the FY 2003/04.

**FINDING 6 —  
Property tax  
administrative costs**

The administrative costs for property tax functions for this audit period appear to have been properly computed, but when the pro rata share attributable to all local agencies were computed for FY 2001-02, the county failed to include all property tax revenue sources in the computation. This oversight resulted in some agencies paying a slightly larger or slightly smaller share than if the shares had been computed properly.

Requirements for the reimbursement of county property tax administrative costs are found in *Revenue and Taxation Code* Section 95.3. County property tax administrative costs are incurred by the assessor, the tax collector, the assessment appeals board, and the auditor. The county is allowed, depending on the fiscal year and any corresponding exclusions, to be reimbursed by local agencies and public schools for these administrative costs.

Recommendation

The amount of over/underpayment for FY 2001-02 was determined to be immaterial for all affected agencies, but because this process is repeated annually, the county must correct this computation procedure for all future years.

County's Response

**Response:** The distribution of the Administrative Cost should have included the weighted average of the Unitary and Secured apportionment factors. Our office used the Secured factors to apportion the Costs; we should have also included the Unitary factors in the distribution.

**Action:** The past apportionments of the Costs have been recalculated using the weighted average of the Secured and Unitary factors. The variances will be included when our office calculates the FY 2003/04 Costs.

## **San Francisco County (July 1, 1998, through June 30, 2001)**

**Follow-up on Prior  
Audit Findings**

Findings noted in the prior audit report, dated July 28, 1999, have been satisfactorily resolved by the county.

**FINDING 1—  
Supplemental  
property tax**

The county apportioned the supplemental property tax revenues quarterly rather than 30 calendar days after the close of the preceding monthly or four-week accounting period.

The county did not allocate supplemental property tax incremental revenues to the redevelopment agencies (RDAs).

The legal requirements for supplemental roll property tax apportionment and allocation are found in *Revenue and Taxation Code* Sections 75.60 through 75.71 and 100.2. When there is a change in assessed property value due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

Recommendation

The county must apportion the supplemental property tax revenues in accordance with *Revenue and Taxation Code* Section 75.60 and apportion all eligible tax increments within the RDA projects to the RDA agencies.

County's Response

We concur with the recommendation to apportion the supplemental property tax revenues on a monthly basis as required under *Revenue and Taxation Code* Section 75.70 and allocate all supplemental property tax incremental revenues within the redevelopment projects to Redevelopment Agency (RDA). We have implemented this finding, effective in Fiscal Year 2002-03.

**FINDING 2—  
Redevelopment  
agencies (RDA)**

The county did not allocate the actual net requirement or 100% of eligible property tax revenue increments to the RDAs.

The auditors found that the RDA's calculation of the 2% pass-through for projects created after January 1994 includes ERAF. In addition, the ERAF portion received by the county was deposited into the general county funds.

Requirements for the apportionment and allocation of property tax to RDAs are found in *Revenue and Taxation Code* Sections 96.4 and 96.5. California Community Redevelopment Law generally entitles a community redevelopment agency to all of the property tax revenues that are realized from growth in values since the redevelopment project's inception.

Recommendation

The county must establish the correct net requirements for the RDAs and apportion the net requirement or 100% of eligible property tax revenue increments, whichever is less.

The county must return the ERAF pass-through amount to the RDA. In addition, the county must inform the RDA to correct the pass-through formula and re-apportion the incorrect revenue to the qualified special districts.

County's Response

We concur that the County must calculate the full allocation to Redevelopment Agency pursuant to *Revenue and Taxation Code* Sections 96.4 and 96.5. However, it is the policy of the City and County of San Francisco to actually allocate the Agency's annual budget as approved by the Board of Supervisors during the budget process. Based on a legal opinion rendered by the County's Counsel on this matter, the adoption of the annual budget by the Board constitutes indebtedness for the purpose of using tax increments to pay for the Agency's expenditures. The County will be reviewing and sharing this audit finding with the County's Counsel to once again review the appropriateness of the existing practice.

**FINDING 3—  
Unitary and operating  
nonunitary  
apportionment**

The county incorrectly apportioned the unitary and operating nonunitary revenues by using a different formula for the RDAs. In addition, the apportionment process is multiplied by the regular secured tax rate, rather than by a unitary and operating nonunitary tax rate, to obtain the proportionate share of each agency.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in *Revenue and Taxation Code* Section 100.

Unitary properties are those properties on which the Board of Equalization “may apply the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee” (i.e., public utilities and railroads). The *Revenue and Taxation Code* further states, “Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee.”

In FY 1988-89, the Legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The unitary and operating nonunitary base year was established and formulas were developed to compute the distribution factors for the fiscal years that followed.

Recommendation

The county must include the RDAs in the unitary and operating nonunitary apportionment factor calculation and multiply all the jurisdiction factors by a unitary and operating nonunitary tax rate.

County’s Response

We agree with your finding. The County has recalculated and included the Redevelopment Agency’s project areas in the unitary and operating non-unitary apportionment factors for allocation of unitary property tax revenues to all taxing jurisdictions.

**FINDING 4—  
Educational Revenue  
Augmentation Fund  
(ERAF)**

The county incorrectly provided general fund revenues to the ERAF for an RDA ERAF shift. In addition, the county improperly reduced the ERAF factor and transferred the factor to the library fund (Schedule 1).

For the period of July 1, 1997, through June 30, 2001, the county overallocated \$8,309,123 to the ERAF. However, *Revenue and Taxation Code* Section 96.1 limits the maximum adjustment to the ERAF to 1% of the FY 2001-02 secured property tax levy. Information provided by the county indicates that the FY 2001-02 secured levy was \$914,785,493. Thus, the maximum adjustment to ERAF is \$9,147,855. Therefore, the maximum payment from the ERAF is limited to the overallocated amount of \$8,309,123.

Recommendation

The county must correct the AB 8 system and the unitary and operating nonunitary system. For the AB 8 system, the general fund should not



provide an ERAF shift for the redevelopment agencies and the ERAF factor that was given to the library fund must be returned to the ERAF. For the unitary and operating nonunitary system, the apportionment factor must be computed separately from the AB 8 system and all new districts must be added when revenue exceeds 102%. Once the systems are corrected, the county must retroactively correct the ERAF shift.

#### County's Response

We concur with your audit finding that the County's general fund over-allocated \$8,309,123 to ERAF for the period of July 1, 1997 through June 30, 2001. The County has corrected both the AB 8 allocation factors and the unitary and operating non-unitary factors. This \$8,309,123 will be deducted from the FY 2002-03 ERAF property tax distributions and will be noted in our April reports to the California Department of Education and the California Community Colleges. In addition, the County has adjusted the ERAF factor that was given to the County's Library Fund and will retroactively correct the ERAF shift.

This is in response to your draft audit report dated April 8, 2003 on property tax apportionment and allocation system for the period of July 1, 1998 through June 30, 2001. All audit findings listed have been addressed in our letter to you dated February 18, 2003 except for the additional finding on Redevelopment Agency statutory pass-through, which included ERAF in its computations. The County informed RDA and is in agreement with the audit finding. The Agency corrected the pass-through calculations excluding ERAF and will re-apportion the pass-through amounts to eligible taxing entities. Both the County and RDA will do the necessary adjustments.

## **Santa Barbara County (July 1, 1998, through June 30, 2002)**

### **Follow-Up on Prior Audit Findings**

Findings noted in the prior audit report, dated July 30, 1999, have been satisfactorily resolved by the county.

### **FINDING— Educational Revenue Augmentation Fund (ERAF)**

The FY 1999-2000 ERAF shift amount was not properly carried forward to FY 2000-01 as required. The amount carried forward in FY 2000-01 was reduced by \$2,394. The reduction was the result of using an out-of-balance increment report to obtain the taxes for two jurisdictional changes (Schedule 1).

During the audit, the county corrected the two jurisdictional change computations using the appropriate increment report.

#### Recommendation

The corrected allocations should be input into the system prior to the new year rollover so that the prior-year tax amounts will be properly allocated.

#### County's Response

We concur with the finding and have made the appropriate corrections per your recommendation.

## Sierra County (July 1, 1997, through June 30, 2003)

### Follow-up on Prior Audit Findings

Findings noted in the prior audit report, dated April 1, 1998, have been satisfactorily resolved by the county.

### FINDING 1— Calculation and distribution of ATI

At the beginning of the FY 2002-03 annual tax increment (ATI) process, the county failed to carry the prior year assessed values forward to compute the current increment and also failed to carry forward the prior year gross revenue. The net result is that the FY 2002-03 gross revenue is correct, but the ERAF computations are misstated because two years of growth were computed and reflected in the ERAF growth percentages.

Requirements for the apportionment and allocation of the ATI are found in *Revenue and Taxation Code* Sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to TRAs on the basis of each TRA's share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction's ATI factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The ATI is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

#### Recommendation

The county has computed corrected ATI revenue, growth, and ERAF amounts for FY 2003-04 that will include the prior year revenue adjustments and corrected prior year revenue amounts to be used for the FY 2003-04 ATI and ERAF process.

### FINDING 2— Unitary and operating nonunitary apportionment

The county unitary revenue growth amount in excess of 102% for FY 1997-98 was not computed properly. The excess over 102% was computed and apportioned by AB 8 factors before ERAF adjustments. Therefore, the ERAF was not included in the calculation and all ERAF-contributing agencies were overpaid. Since the same factors were used for the pipeline right-of-way tax apportionment, they were also in error. This error is carried through all years of this audit. The County Auditor has accepted this finding, but does not find any justification to include the ERAF in the unitary and operating nonunitary computations in the prevailing statutes, and would like clarification from the SCO regarding the inclusion of the ERAF in the growth computation.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in *Revenue and Taxation Code* Section 100.

Unitary properties are those properties on which the Board of Equalization "may apply the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities and railroads). The *Revenue and Taxation Code* further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the Legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The unitary and operating nonunitary base year was established and formulas were developed to compute the distribution factors for the fiscal years that followed.

#### Recommendation

The county has computed corrected unitary revenue amounts for all years and is prepared to implement those corrections in FY 2003-04 if required. The issue has been referred to SCO legal council for clarification.

### **FINDING 3— Educational Revenue Augmentation Fund (ERAF)**

The ERAF corrections from the prior audit were not fully implemented for the first year of this audit (FY 1997-98), resulting in incorrect ERAF computations for all years of this audit. There was also an error noted in the growth formula for the City of Loyalton per capita computation (see Schedule 1).

Requirements for the local agency shift of property tax revenues to the ERAF are generally found in *Revenue and Taxation Code* Sections 97.1 through 97.3. Beginning in FY 1992-93, each local agency was generally required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF are subsequently allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was generally determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was generally determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts was generally determined by shifting the lesser of 10% of that district's total annual revenues as shown in the FY 1989-90 edition of the State Controller's *Report on Financial Transactions Concerning Special Districts* or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties was generally determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, was generally determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting this amount by subtracting the FY 1992-93 shift to the ERAF;

- If the above amount is greater than zero, adjusting this amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding this amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift was generally determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;
- Adjusting this amount for growth; and
- Adding this amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years subsequent to FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

#### Recommendation

The county has computed FY 2003-04 ERAF spreadsheets and revenue adjustments to correct all prior errors noted.

## **Siskiyou County (July 1, 1995, through June 30, 2001)**

### **Follow-up on Prior Audit Findings**

Findings noted in the prior audit report, dated February 28, 1997, have been satisfactorily resolved by the county.

### **FINDING 1— Calculation and distribution of ATI**

In fiscal year (FY) 2000-01, the county incorrectly computed the annual tax increment (ATI) for the Mayten, Montague, Mt. Shasta, Scott Valley, and South Yreka fire districts. The ATIs by tax rate area (TRA) were incorrectly carried forward to the AB 8 summary.

Requirements for the apportionment and allocation of the ATI are found in *Revenue and Taxation Code* Sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to TRAs on the basis of each TRA's share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction's annual tax increment apportionment factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

Recommendation

The county corrected this error during the audit period and recomputed all apportionments to properly reflect the correction. No further action is required by the county.

County's Response

Corrected at time of audit. Process implemented to flag similar situations and prevent a similar error in the future.

**FINDING 2—  
Jurisdictional changes**

The county incorrectly adjusted the assessed values for the South End and Gretchen annexations in FY 1999-2000.

The legal requirements for jurisdictional changes are found in *Revenue and Taxation Code* Section 99. A jurisdictional change involves a change in organization or boundaries of local government agencies and school districts. Normally, these are service area or responsibility changes between the local jurisdictions. As part of the jurisdictional change, the local government agencies are required to negotiate any exchange of base year property tax revenue and annual tax increment. After the jurisdictional change, the local agency whose responsibility increased receives an additional annual tax increment, and the base property tax revenues are adjusted according to the negotiated agreements.

Recommendation

The county corrected this error during the audit period by readjusting the assessed valuations for these districts. No further action is required by the county.

County's Response

Corrected at time of audit. Process implemented to flag similar situations and prevent a similar error in the future.

**FINDING 3—  
Unitary and  
operating nonunitary  
apportionment**

The county incorrectly computed the unitary apportionment factors in FY 2000-01. The base year revenue in FY 1999-2000 was incorrectly carried forward in FY 2000-01, resulting in incorrect apportionment factors for FY 2000-01.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in *Revenue and Taxation Code* Section 100.

Unitary properties are those properties on which the Board of Equalization “may apply the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee” (i.e., public utilities and railroads). The *Revenue and Taxation Code* further states, “Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee.”

In FY 1988-89, the Legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The unitary and operating nonunitary base year was established and formulas were developed to compute the distribution factors for the fiscal years that followed.

#### Recommendation

The county corrected this error during the audit period and recomputed all apportionments to properly reflect the correction. No further action is required by the county.

#### County's Response

Corrected at time of audit. Process implemented to flag similar situations and prevent a similar error in the future.

### **FINDING 4— Educational Revenue Augmentation Fund (ERAF)**

The method used by the county to implement AB 1519 permanently reduced the county fire district ERAF shift by the California Department of Finance computation of \$3,857. As a result, the county underallocated ERAF by \$27,400 (adjusted for growth) (Schedule 1).

Requirements for the local agency shift of property tax revenues to the ERAF are generally found in *Revenue and Taxation Code* Sections 97.1 through 97.3. Beginning in FY 1992-93, each local agency was generally required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF are subsequently allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was generally determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was generally determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts was generally determined by shifting the lesser of 10% of that district's total annual revenues as shown in the FY 1989-90 edition of the State Controller's *Report on Financial Transactions Concerning Special Districts* or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties was generally determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, was generally determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting this amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting this amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding this amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift was generally determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;
- Adjusting this amount for growth; and
- Adding this amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years subsequent to FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

For the period of July 1, 1995, through June 30, 2001, the county underallocated \$27,440 to the ERAF. *Revenue and Taxation Code* Section 96.1(c) limits the maximum adjustment to the ERAF to 1% of the current year's original secured roll tax levy. Information provided by the county indicated that the audit finding is less than 1% of the current year's original secured roll tax levy. Since the audit adjustment is less than the maximum, this *Revenue and Taxation Code* section does not apply.

#### Recommendation

The county should transfer \$27,440 to the ERAF and adjust future ERAF shift computations to reflect the loss of the ERAF shift adjustment.

County's Response

The County of Siskiyou does not agree with this finding. The Controller's position is that the intent of AB1519 was a one-year adjustment. It is our contention that it was a permanent adjustment based on the same intent of other fire related "reverse shifts" that was happening at that time. The County of Siskiyou will transfer the appropriate funds (\$27,440) to an escrow account and subsequent years as well. These funds will remain in the County of Siskiyou treasury until this matter is resolved.

SCO's Comment

SCO legal counsel has opined:

The language of Section 97.31 clearly states that for each eligible county, the county auditor may submit the necessary information by November 1, 1993 and the Director of Finance shall, by January 15, 1994 notify each county of its reduction in its amount to be transferred to the Education Revenue Augmentation Fund. There are no provisions for submission of the information after those particular dates nor further calculations to be done by the Director of Finance. The director of Finance shall notify each county of its reduction by January 15, 1994, which is a one-time notification and therefore it appears that the language within this Section does not support shift reductions in other years. By selecting specific dates, the language of the statute clearly emphasizes this as a one-year reduction.

Further, the language of 97.31(a)(1) clearly states that "the total amount of the reductions for all counties shall not exceed two million dollars." This \$2,000,000.00 statewide cap is applicable for fiscal year 1993-1994.

As the shift reduction is a one-year reduction, it stands to reason that counties cannot compute a growth amount on the shift reduction in subsequent years.

Therefore, the finding remains as written.

## **Sonoma County (July 1, 1999, through June 30, 2002)**

### **Follow-up on Prior Audit Findings**

Findings noted in the prior audit report, dated February 14, 2000, have been satisfactorily resolved by the county.

The audit disclosed that the county complied with California statutes for the allocation and apportionment of property tax revenues for the period audited.



## Sutter County (July 1, 1997, through June 30, 2002)

### Follow-up on Prior Audit Findings

Findings noted in the prior audit report, dated June 17, 1998, have been satisfactorily resolved by the county.

### FINDING— Supplemental property tax – administrative costs

The county did not document the cost of assessing, billing, collecting, and apportioning supplemental taxes to justify the collection of the 5% administrative fee in fiscal year (FY) 1999-2000, FY 2000-01, and FY 2001-02. In prior years, the county has documented these costs. Through FY 1998-99, the county has documented costs that exceeded the allowable administrative fee and have a carryover reimbursement balance in excess of \$680,000.

*Revenue and Taxation Code* Section 75.60 allows a county to charge an administrative fee for supplemental property tax collections. This fee is not to exceed the lesser of 5% of the supplemental property taxes collected or the actual administrative costs.

### Recommendation

The county should provide, for all years of the audit period, documentation of supplemental costs to support the 5% administrative fee collected. Failure to provide the necessary documentation will result in the disallowance of future claimed costs.

### County's Response

We have compiled documentation related to the audit period which provides justification for the 5% administration fee. In the future, we will accumulate documentation for this fee on an on-going basis.

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*Copies of the audit reports referred to in this report may be obtained by contacting:*

**State Controller's Office  
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